

after divestiture.<sup>49</sup> Today, cable lines pass 88 million homes representing 96 percent of all television households (90 percent of all households) in the United States, and some 62 percent of those households (54.5 million) actually subscribe to cable service.<sup>50</sup> TCI, the largest cable company, controls cable access to over 10 million subscribers.<sup>51</sup> Congress has found that the cable industry has become highly concentrated and that most cable companies exercise market power in their own service areas.<sup>52</sup>

As evidenced by the recently announced joint venture between US WEST and Time Warner, the cable industry is now moving fast toward two-way capabilities and a head-on chal-

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<sup>49</sup>Cable Communications Policy Act of 1984, Pub. L. No. 98-549, 98 Stat. 2789 (1984), codified in 47 U.S.C.A. §§ 521-559 (West Supp. 1991).

<sup>50</sup>NCTA, Cable Television Developments 1-A (Mar. 1993).

<sup>51</sup>Id. at 14-A.

<sup>52</sup>Pub. L. No. 102-385 §2(4) Findings, Policy, Definitions (Oct. 5, 1992). Most cable franchises face no direct competition within their service areas from other cable providers. Of the approximately 10,000 cable systems in the U.S., only about 60 communities have head-to-head cable competition. Justice Department economists attribute 40 to 50 percent of the rise in price of cable service since deregulation to the exercise of market power. R. Rubinovitz, Dep't of Justice, Economic Analysis Group Discussion Paper No. EAG 91-8, Market Power and Price Increases for Basic Cable Service Since Deregulation 2 (Aug. 6, 1991).

In the handful of communities that allow head-to-head cable competition, basic rates are one third lower than elsewhere. Affidavit of Thomas W. Hazlett at 8, United States v. Western Elec. Co., CA Dkt. No. 82-0192 (D.D.C. Jan. 9, 1991).

lenge to local telephone companies.<sup>53</sup> Cable companies are replacing their "tree and branch" networks with "star" configurations that use the more efficient fiber optic lines to connect the cable head-end to a neighborhood node, and coaxial cable to serve the homes themselves.<sup>54</sup> Interactive cable television is already a functioning reality in a number of U.S. test markets,<sup>55</sup> and is available to 200,000 sub-

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<sup>53</sup>G. Gilder, Cable's Secret Weapon, Forbes, Apr. 13, 1992, at 80.

<sup>54</sup>Id. at 80-81.

<sup>55</sup>Interactive Network Inc., a Mountain View, California, firm that has tested its programming in 200 cable homes in Sacramento, California, has attracted investments from a number of media companies, including NBC, Cablevision Systems and A. C. Nielsen Co. Interactive Network's trial service began in March 1992 using proprietary hardware and FM radio signals exclusively to provide two-way services. C. Moosakis, Which Way for Two-Way, Cablevision, Aug. 27, 1990, at 17; Clifford, 2-Way Television Testing Under Way by Peninsula Firm, San Francisco Bus. Times, May 29, 1992, § 1, at 1.

ACTV Inc., owned by New York advertising agency McCann Erickson, recently completed a test of its programming-based service to cable subscribers in Springfield, Massachusetts, and is raising \$100 million for a national cable-delivered service in which ACTV would be paired with the Canadian Videoway. ACTV technology employs four cable channels, decoder boxes with semiconductor chips and tuners to provide seamless switching from the company to the viewers' remote controls. C. Moosakis, Which Way for Two-Way, Cablevision, Aug. 27, 1990; K. Harris, MTV Whiz Jumps from Hyperactive to Interactive, L.A. Times, June 7, 1992, at D1.

TV Answer, a Reston, Virginia, based firm, uses radio waves to provide its two way services. This Isn't the Response TV Answer Expected, Business Week, June 29, 1992, at 78; P. Wiseman, Have Bills to Pay, Turn on Your TV, USA Today, July 9, 1992, at B2.

scribers in Canada and the United Kingdom.<sup>56</sup>

Cable carriers are now forging a number of key new alliances in preparation for direct, head-to-head competition with local telephone companies. Cable-CAP consortia are deploying fiber-optic cable at record rates, and are aggressively developing the new-generation radio services. By combining their competitive transport facilities with local telephone company switching capabilities, the cable-CAPs will soon be presenting themselves to customers as fully competitive local exchange carriers offering switched service and a full panoply of competitive enhancements.<sup>57</sup>

The cable-CAP consortia are in turn allying themselves with providers of cellular and PCS radio services.<sup>58</sup> The high-capacity trunks that cable-CAP companies operate are per-

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<sup>56</sup>Multimedia: Videoway Adds Fast-Trax VD-1 Technology for Enhanced Multimedia & Transactional Services, Edge: On & About AT&T, May 11, 1992. Le Groupe Videotron, Canada's second-largest multi-system operator (MSO), introduced its Videoway package of interactive services to Montreal cable subscribers in 1991. T. Kerver, Realizing New Revenues, Cablevision, June 18, 1990, at 68. A button on the remote control feeds the viewer's response back to the cable company.

<sup>57</sup>Recently, Teleport, a leading CAP, announced a joint venture with eleven cable companies. Under the agreement, the cable companies will expand their networks into business areas and Teleport will utilize these networks in offering a broad range of telecommunications services. J. Mulqueen, Teleport Expands Bounds--Enters Partnerships with 11 Cable TV Companies to Reach Business Markets, Communications Daily, June 21, 1993, at 3A.

<sup>58</sup>Sixty-five cable television companies have formed Cable Television Laboratories, an information-sharing alliance with P.C.N. America. E. Andrews, Cable TV in Phone Challenge, N.Y. Times, Feb. 28, 1991, at D1.

fectly suited to serve as backbone networks; they can knit together cell sites and mobile switches, link mobile switches into local and regional networks, and connect them to long-distance carriers.<sup>59</sup>

Summary. Large business customers are already benefiting from a great deal of competition in the local exchange. To be sure, today's small residential and business customers remain largely dependent on the single, established local exchange carrier for telephone service. But even that residual core of the local exchange monopoly will not survive much longer. Cable-CAP-radio companies are now poised to offer house-to-house and business-to-business phone service in direct competition with local telephone companies.

Increasingly, both large and small customers want end-to-end service from a single provider. In the years ahead, there will be a number of such vertically-integrated providers (or coalitions of providers) from which to choose. FCC initiatives will permit CAPs, interLATA carriers, cable operators, and radio providers to meet the demand for end-to-end service.

The counterpart of those initiatives should be relief for the BOCs to provide interLATA services, so that they, too, can compete on an equal basis. Given an appropriate regulatory framework, there can be no serious concern that local carriers

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<sup>59</sup>PacTel Cellular Detroit, for example, uses a combination of leased fiber and microwave for its network and has replaced some BOC-provided local loop circuits with leased cable TV fiber to IXC facilities.

will somehow recapture all of telecommunications, end to end. The regulatory challenge now is not to guard against the obsolete specter of all-consuming monopoly, but to construct a new regulatory paradigm that can properly accommodate full-fledged competition in the interstate long distance telecommunications business, as well as the competition developing within the States. It is to that challenge that the proposed rulemaking is addressed. The BOCs accordingly ask the Commission to find that BOC provision of interLATA services would be in the public interest.

**B. The Commission Already Has In Place Many If Not Most Of The Regulatory Mechanisms Necessary To Govern BOC InterLATA Services And To Prevent Discrimination And Cross-Subsidy**

In 1987, the Commission mentioned six specific issues that it would have to consider prior to BOC entry into interLATA services: "(1) modifications to the Competitive Carrier dominant/nondominant classifications; (2) the proper degree of separation (structural or accounting); (3) rate of return treatment for BOC interexchange services; (4) access charge treatment when a BOC resells the services of an unaffiliated interexchange carrier; (5) disclosure rules for network and customer proprietary information; and (6) application of the requirement of equal access, and possibly CEI and ONA requirements, to ensure fair competition when a BOC offers interLATA

services."<sup>60</sup> The list was not intended to be exhaustive. The Commission stressed that "BOC entry into interexchange markets currently proscribed by the decree raises many issues that this Commission must address independently prior to such BOC entry."<sup>61</sup>

The Commission already has experience regulating BOC provision of interLATA services. BOCs have been engaged in the provision of some interLATA services since divestiture.<sup>62</sup> The Commission also has experience with the far more extensive interLATA services offered by other Tier 1 LECs such as GTE and United Telephone (Sprint).<sup>63</sup> Moreover, the same core cluster of issues -- equal access, access charges, cost accounting, network disclosure, CPNI -- arise in the context of BOC provision of enhanced services and customer premises equipment. As the Commission explained to the district court in 1987:

we already have available the regulatory mechanisms that will be needed to oversee BOC participation in

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<sup>60</sup>Comments of the FCC on the Report and Recommendations of the U.S. Concerning the Line of Business Restrictions at 30 (Mar. 13, 1987).

<sup>61</sup>Ibid.

<sup>62</sup>The Local Access and Transport Areas (LATAs) configured to implement the MFJ occasionally cross state boundaries. Hence, most BOCs provide some interstate intraLATA service. In addition, Bell Atlantic and NYNEX telephone companies provide interLATA service under a "corridor" traffic exception to the decree restraints.

<sup>63</sup>Application of GTE Corp. (Southern Pacific Transfer), 94 F.C.C.2d 235 (1983); United Telecommunications, Inc., 98 F.C.C.2d 1306 (1984).

this marketplace to ensure that no harm results to the public or to competition. Many of the regulatory mechanisms already prescribed for other BOC activities or other carriers -- such as cost accounting requirements, nondiscrimination provisions, access charge guidelines, and equal access requirements -- are readily adaptable to BOC interstate interexchange offerings.<sup>64</sup>

In what follows, we identify the key issues that bear directly on the proposed rulemaking. We have broken those issues down under two headings -- discrimination and cross-subsidy -- to focus on the underlying concerns to which the regulatory safeguards are addressed. It will be quickly apparent, as the Commission has already noted, that most of the regulatory mechanisms necessary to govern BOC participation in interLATA markets are already in place. What is needed, for the most part, is simply an express application of existing regulatory mechanisms to BOC participation in interLATA competition.

**1. Safeguards Against Discrimination.** The Commission has identified three issues -- equal access, network disclosure, and the use of customer proprietary information -- that bear on the problem of discrimination. All of these issues have been fully explored in other proceedings. The Commission may well conclude, therefore, that what is needed in this proceeding is the express extension of existing rules to govern BOC entry into new markets.

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<sup>64</sup>Reply Comments of the FCC on the Report and Recommendations of the U.S. Concerning the Line of Business Restrictions (May 22, 1987).

Equal access. The Commission has had almost a decade of experience with equal access for interLATA carriers, including experience ensuring that equal access is provided by exchange carriers that are also in the interexchange business. The basic principles of equal access are well established. They are already functioning smoothly and are unlikely to be affected by BOC provision of interLATA services.

The AT&T consent decree placed an "equal access" requirement on all the BOCs.<sup>65</sup> By 1985, scarcely a year after divestiture, the Commission had adopted and implemented equal access rules of its own. The Commission directed all local exchange carriers (not just the former AT&T affiliates) to undertake equal access conversions.<sup>66</sup> The Commission further "require[d] any exchange carrier offering interexchange service to impute to itself the same costs that it uses to develop the access rates that it charges its interexchange customers."<sup>67</sup> And, specifically with respect to BOC interLATA

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<sup>65</sup>MFJ § II(A) and Appendix B. See also United States v. Western Electric Co., 569 F.Supp. 1057, 1063 (D.D.C. 1983) (defining equal access as access "whose overall quality in a particular area is equal within a reasonable range which is applicable to all carriers").

<sup>66</sup>MTS and WATS Market Structure, Phase III, 100 F.C.C.2d 860, 877 (1985) (hereinafter Phase III); Investigation into the Quality of Equal Access Services, 60 Rad. Reg.2d (P & F) 417, 419 (1986) (hereinafter Equal Access Quality Investigation).

<sup>67</sup>Policy and Rules Concerning Rates for Dominant Carriers, 6 F.C.C. Rcd 2637, 2714 (1991).



services, the Commission has established that a BOC must acquire access from the same tariffs as its competitors.<sup>68</sup>

The FCC has regularly monitored the quality and price of access offered by the exchange carriers. In its most recent Trends in Telephone Service report, the FCC has noted that the BOCs have converted well over 95% of their lines to equal access, and that about 90% of the nation's telephone lines, overall, have made the transition.<sup>69</sup> The only obstacles to 100% coverage are the continued existence of primitive switches in some end offices and the lack of an alternative long-distance carrier serving some rural areas. But the basic principles of equal access are well established, and the Commission has clear benchmarks at hand for judging future performance.<sup>70</sup>

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<sup>68</sup>Application of Access Charges to the Origination and Termination of Interstate, IntraLATA Services and Corridor Services, FCC No. 85-172 (Apr. 12, 1985).

<sup>69</sup>Industry Analysis Div., FCC, Trends in Telephone Service 16 (Sept. 16, 1992).

<sup>70</sup>As the D.C. Circuit recently explained:

The seven independent BOCs are not the old AT&T.  
\* \* \* [T]he existence of seven BOCs increases the number of benchmarks that can be used by regulators to detect discriminatory pricing. \* \* \* Indeed, federal and state regulators have in fact used such benchmarks in evaluating compliance with equal access requirements \* \* \* and in comparing installation and maintenance practices for customer premises equipment.

United States v. Western Elec. Co., No. 91-5263, slip op. at 20.

Moreover, the Exchange Carrier Standards Association, composed of both exchange and interexchange carriers, was organized in early 1985 under the auspices of the American National Standards Institute; its Carrier Liaison Committee provides an open forum for the resolution of equal access interconnection problems.<sup>71</sup> The Committee's Network Operations Forum resolves provisioning problems (matters involving installation, repair, and maintenance), while its Interexchange Customer Service Center resolves exchange access ordering problems.<sup>72</sup> These forums address national issues; local problems are resolved bilaterally.<sup>73</sup> The FCC monitors the entire process and provides regulatory review when necessary.<sup>74</sup> In particular, the Commission has continued to grapple with the question of how equal is "equal."<sup>75</sup> Investigations have examined such matters as call blocking frequencies, the sufficiency of access trunks, trunk selection methods, and the transmission quality of access services. Any or all of these well-established procedures could be

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<sup>71</sup>Phase III, 100 F.C.C.2d at 861, 880-883, 882 n.72; MTS and WATS Market Structure, Phase III, 58 Rad. Reg.2d (P & F) 731, 733 (1985) (hereinafter Market Structure).

<sup>72</sup>Phase III, 100 F.C.C.2d at 883-884; Market Structure, 58 Rad. Reg.2d at 733-734, 740.

<sup>73</sup>Market Structure, 58 Rad. Reg.2d at 733.

<sup>74</sup>See Phase III, 100 F.C.C.2d at 884. See also Market Structure, 58 Rad. Reg.2d at 739.

<sup>75</sup>See, e.g., Equal Access Quality Investigation, 60 Rad. Reg.2d at 417.

relied on to assure the continuation of truly equal access following BOC entry into the interLATA market.

Network Information Disclosure. Existing rules already require the BOCs to inform interLATA carriers, in advance, about any new or modified network interfaces or services affecting interconnection to the network. Under the Commission's "All Carrier Rule," all carriers are obliged to make information necessary to intercarrier interconnection available in a timely manner and on a reasonable basis.<sup>76</sup>

In addition to this broad requirement, the Commission has adopted more specific rules governing disclosure of information for the interconnection of CPE (47 C.F.R. Section 68.110(a) and (b)) and enhanced services (47 C.F.R. Section 64.702).<sup>77</sup> Since new or modified network configurations affecting CPE and enhanced services would almost invariably

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<sup>76</sup>In re Computer and Business Equipment Manufacturers Association, 93 F.C.C.2d 1226, 1228 (1983) (citing Amendment of Section 64.702 of the Commission's Rules and Regulations (Second Computer Inquiry), 84 F.C.C.2d 50, 82 (1980)) (ordering carriers owning basic transmission facilities to disclose all areas of information (network design, technical standards, research and development, customer proprietary, etc.) to "all interested parties on the same terms and conditions insofar as such information affects either intercarrier connection or the manner in which interconnected CPE operates"). See also Amendment of Sections 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry), 104 F.C.C.2d 958, 1080-1086 (1986) (hereinafter Computer III).

<sup>77</sup>Disclosure must take place either six months before the proposed change in network design or at the "make/buy" point -- the point at which the BOC decides to manufacture itself, or to purchase from another company, any product that affects the network interface -- whichever is earlier. Computer III, 104 F.C.C.2d at 1086.

affect interLATA services as well, these more specific rules apply, as a practical matter, to network changes affecting interLATA services. The Commission may, however, wish to consider making that application explicit.

CPNI. The Commission has carefully designed CPNI rules in the enhanced services context to balance competing concerns of efficiency, competitive equity, and privacy. In general, these rules require BOCs to:

- (a) make CPNI available, upon a customer's request, to unaffiliated ESPs;
- (b) prevent BOC personnel who market enhanced services from accessing a customer's CPNI, if the customer "blocks";
- (c) prevent BOC personnel who market enhanced services from accessing CPNI of customers with more than 20 lines, without prior written authorization;
- (d) provide unaffiliated ESPs with aggregate CPNI which BOCs provide to their own personnel who market enhanced services; and
- (e) notify multi-line business customers of their CPNI rights.<sup>78</sup>

These rules could be reviewed for their applicability to BOC provision of interLATA services.

**2. Safeguards Against Cross-Subsidy.** The cluster of inter-related issues concerning cross-subsidy that the Commission may address are (1) what degree of separation (structural or accounting) is to be imposed on the BOCs' interLATA operations; (2) whether the BOCs' interLATA

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<sup>78</sup>Amendment of Section 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry), 3 F.C.C. Rcd 1150, 1161 (1988).

operations are to be treated as dominant and therefore subjected to complete Title II regulation; and (3) what sort of pricing regulation will govern BOC charges for interLATA services.

The general rule established in the Commission's Competitive Carrier Proceeding is that domestic, interstate affiliates of LECs are treated as non-dominant carriers and need not structurally separate their local and interstate operations.<sup>79</sup> They must, however, keep separate books of account, and the interLATA operations must take affiliated local services under tariff.<sup>80</sup>

In 1984, however, the Commission indicated that, in an excess of caution, it would "regulate the BOCs' interstate, interLATA services as dominant until we determine[] what degree of separation, if any, would be necessary for the BOCs or their affiliates to qualify for nondominant regulation."<sup>81</sup> And, in 1987, the Commission intimated that, as dominant carriers, the BOCs would be "required to provide \* \* \* inter-LATA services through a structurally separated affiliate."<sup>82</sup>

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<sup>79</sup>Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefor, 98 F.C.C.2d 1191, 1200 (1984) (hereinafter Competitive Common Carrier Proceeding).

<sup>80</sup>Id. at 1198.

<sup>81</sup>Id. at 1198 n.23.

<sup>82</sup>Comments of the FCC on the Report and Recommendations of the U.S. Concerning the Line of Business Restrictions at 28-29 (Mar. 13, 1987). The basis for this statement is unclear. Nothing in the Competitive Common Carrier Proceeding indicated

Revisiting these issues is clearly in order; market and regulatory conditions have changed fundamentally since 1987. The Commission has recognized, for example, that in the competitive environment now prevailing the costs of structural separation for BOC provision of CPE and enhanced services outweigh the benefits. In place of structural separation, the Commission has developed an elaborate set of non-structural safeguards, including detailed accounting rules. The Commission has adopted price caps for BOC access charges and for AT&T's interLATA operations. The Commission has also adopted streamlined regulation of most aspects of AT&T's interLATA operations.

In light of these changes, the Commission should decide that non-structural safeguards, of the sort developed for CPE and enhanced services, will suffice in the context of BOC provision of interLATA services. Permitting the BOCs to integrate their local and long distance activities would not impair Commission efforts to prevent cross-subsidization. As an initial matter, the application of price caps to BOC access services has greatly reduced the incentive for cross-subsidy. "Under price cap regulation," the Commission has explained,

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that structural separation follows automatically from dominant carrier status. To the contrary, the Commission specifically noted that it had so far declined to impose structural separation requirements on the interLATA activities of any local exchange carriers, including the divested BOCs. See Competitive Common Carrier Proceeding, 98 F.C.C.2d at 1197-1198 & n.20.

the BOCs are no longer automatically entitled to increase rates to recoup cost increases as they would have been under a cost-plus, rate of return system of regulation. Instead, rate levels are adjusted to reflect inflation and anticipated efficiency gains by the BOCs. Thus, unlike under rate-of-return regulation, any misallocation of nonregulated costs to regulated operations under price cap regulation normally would not permit higher prices and increased earnings. Rather, any such additional costs would merely reduce BOC earnings.<sup>83</sup>

Price caps, the Commission has thus repeatedly noted, do more than merely strengthen existing deterrents to cross-subsidy. They "substantially decrease incentives to shift costs from more to less competitive service offerings. The rules governing the periodic revision of the caps could reduce, if not eliminate, any perverse incentive to inflate rate bases."<sup>84</sup> As the D.C. Circuit recently noted, "the FCC move in the direction of price cap regulation \* \* \* reduces any BOC's ability to shift costs from unregulated to regulated activities, because the increase in costs for the regulated

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<sup>83</sup>In re Computer III Remand Proceedings, 6 F.C.C. Rcd 174, 178 (1990). The Commission has explained that "segregating LEC access services into four baskets defeats any LEC attempts to finance a predatory rate level by contemporaneously increasing rates for other services." In re Policy and Rules Concerning Rates for Dominant Carriers, 5 F.C.C. Rcd 6786, 6791 (1990).

<sup>84</sup>In re Policy and Rules Concerning Rates for Dominant Carriers, 2 F.C.C. Rcd 5208, 5213 (1987). See also 5 F.C.C. Rcd at 6791 ("Incentive regulation, by in large measure removing the incentive to misallocate costs between services, may mitigate misallocation as a regulatory concern."); In re Computer III Remand Proceedings, 6 F.C.C. Rcd 7571, 7577 (1991) ("price cap regulation for the LECs constitutes an effective complement to cost allocation, reporting, and enforcement safeguards, to reduce BOC incentives to cross-subsidize").

activity does not automatically cause an increase in the legal rate ceiling." United States v. Western Elec. Co., No. 91-5263, slip op. at 20.<sup>85</sup>

In addition to the sharp attenuation of incentives to cross subsidize, the Commission could apply to BOC interLATA activities the accounting rules already in place to allocate costs between jurisdictions under 47 C.F.R. Part 36 and to assign appropriate costs to the interLATA category under 47 C.F.R. § 69.301-410. The cost allocation rules contained in Part 69 include an "interexchange category" comprehensively defined as "services or facilities provided as an integral part of interstate or foreign telecommunications that is not described as 'access service' for purposes of this Part." 47 C.F.R. Section 69.2(s).<sup>86</sup> See also United States v. Western

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<sup>85</sup>See also Statement of Alfred C. Sikes, Chairman FCC, Before the House Subcommittee on Telecommunications and Finance Committee on Energy and Commerce, on FCC Local Exchange Company Price Caps and Regulation and Competition in the Long-Distance Telephone Industry, 1990 FCC LEXIS 4159 (Aug. 2, 1990) ("Under price caps, regulated firms have virtually no ability to pass along cost increases that are within their control. Consequently, concerns regarding anticompetitive cost-shifting and unfair burdening of monopoly ratepayers are drastically reduced.").

<sup>86</sup>The Commission in 1987 indicated that "prior to any BOC entry into interexchange services, this Commission would revisit the adequacy of cost allocation guidelines for separating exchange access and interexchange costs, because they were not originally designed with extensive BOC involvement in interexchange activities in mind." FCC Responsive Comments at 61 n.133 (Apr. 27, 1987). This proceeding would provide the Commission with an opportunity to revisit and revise the guidelines in light of changed conditions, such as the introduction of price caps.



Elec. Co., No. 91-5263, slip op. at 21 ("the FCC has acted since the break-up to tighten its accounting rules, especially its treatment of joint costs, all tending to increase the chances of catching any attempts at cost-shifting").

The Commission could also properly conclude that each BOC's new interLATA operations would be non-dominant. The Commission has defined "dominant carriers as carriers that have market power (i.e., power to control price)." <sup>87</sup> As a new entrant in the interLATA market, a BOC will start with no market share, and thus no power whatsoever to raise prices or restrict output in that market. <sup>88</sup> The Commission has indicated that it will treat "control of bottleneck facilities

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Alternatively, the Commission could apply to BOC provision of interLATA services rules governing separate books and accounts that are akin to the Joint Cost accounting rules, embodied in 47 C.F.R. § 64.901 (allocation of costs) and 47 C.F.R. § 32.27 (affiliate transactions). The Commission stated in 1987 that, "while the Joint Cost Order provides rules for separating regulated and unregulated activities, analogous guidelines might be needed to address cost allocations for interLATA and intraexchange activities." Comments of the FCC on the Report and Recommendations of the U.S. Concerning the Line of Business Restrictions at 29-30 (Mar. 13, 1987). Now that price caps have been implemented, however, and the incentive for cross-subsidy correspondingly reduced, such elaborate accounting safeguards and the reliance on a fully-distributed-cost methodology may not be necessary for a Title II service like long distance.

<sup>87</sup>In re Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefore, 85 F.C.C.2d 1, 20 (1980).

<sup>88</sup>The market in question here is, of course, the interLATA market. As the D.C. Circuit has explained, in determining whether a BOC poses a threat to impede competition, "it is the 'market [the BOC] seeks to enter' that matters." United States v. Western Elec. Co., 900 F.2d at 296.

as prima facie evidence of market power requiring detailed regulatory scrutiny."<sup>89</sup> But the Commission may well decide, as it has for other Tier 1 LECs, that the nondiscrimination safeguards it has already devised are sufficient to keep BOC control of access facilities from giving the BOCs' market power in interLATA services even without a dominant classification.<sup>90</sup>

How the BOCs will charge for interLATA services raises a related issue. As noted, rate-of-return regulation has been largely supplanted by price caps for access charges. Current price cap regulation would also apply to any rates proposed for a BOC offering of interLATA service (as it does now for AT&T).<sup>91</sup> Indeed, an interLATA basket has already been

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<sup>89</sup>85 F.C.C.2d at 51. "Control of bottleneck facilities is present," the Commission explained, "when a firm or group of firms has sufficient command over some essential commodity or facility in its industry or trade to be able to impede new entrants." Id. at 52.

<sup>90</sup>Moreover, the Commission has found that "the development of shared tenant systems, private networks, and other technologies suggests that competition for access services is increasing." Policy and Rules Concerning Rates for Dominant Carriers, 4 F.C.C. Rcd 2873, 3144-3145 (1989). And, in its special and switched access collocation dockets, the Commission is promoting further competition by requiring LECs to provide either physical or virtual collocation at LEC end offices. Report and Order and Notice of Proposed Rulemaking, Expanded Interconnection with Local Telephone Company Facilities, CC Dkt. Nos. 91-141, 92-222 (F.C.C. Oct. 19, 1992).

<sup>91</sup>47 C.F.R. Sections 61.41 et seq.

established expressly for this purpose.<sup>92</sup> In light of the infusion of new competition by the BOCs themselves, however, the Commission may wish to consider whether further streamlining of the pricing process is in order. If the BOCs are to be treated as non-dominant, then streamlined tariff regulation for interLATA services, of the sort proposed for other non-dominant providers,<sup>93</sup> may be appropriate. Indeed, it may then even be possible to eliminate the residual additional regulation still imposed upon AT&T,<sup>94</sup> the one player that to this point clearly does still dominate the interLATA market.

However the Commission resolves these matters, the key threshold finding has already been made: regulatory oversight can "minimize" the risks of cross-subsidy or predation, and successful predation by the BOCs in interLATA services is

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<sup>92</sup>"To the extent that a local exchange carrier specified in [Section] 61.41(a)(2) or (3) offers interstate interexchange services that are not classified as access services for the purposes of Part 69 of this Chapter, such exchange carrier shall establish a fourth basket for such services." 47 C.F.R. § 61.42(d)(4).

<sup>93</sup>See Notice of Proposed Rulemaking, In the Matter of Tariff Filing Requirements for Nondominant Common Carriers, CC Dkt. No. 93-36 (F.C.C. Feb. 19, 1993).

<sup>94</sup>Obviously, the Commission would save substantial resources if it were able, based on an infusion of new competition, to terminate the AT&T deregulation docket (see, e.g., Competition in the Interstate Interexchange Marketplace, 5 F.C.C. Rcd 2627 (1990)) and to cease the time-consuming review of AT&T's various Tariff 12, Tariff 15 and Tariff 16 offerings. AT&T itself has been vigorously advocating such a result for some time. Bell company entry and the transition to a truly competitive marketplace would provide the occasion.

"unlikel[y]" because of "the competitiveness of the market" and "the likelihood of discovery."<sup>95</sup>

### **Conclusion**

Almost a full decade after divestiture, AT&T remains strongly dominant in the interLATA market. During that period, the Commission has developed a full portfolio of regulations to permit full-fledged competition. Such competition will produce lower prices, better services, and more investment in the telecommunications infrastructure. The Commission has told the Court of Appeals that it is prepared to undertake a rulemaking governing BOC provision of interLATA services. The Court of Appeals has expressly invited the Commission to proceed.

Given the rapid pace of change in the telecommunications industry, the decree's interLATA prohibition will be removed. The question is not whether the Commission must act on this matter, but simply when it will do so. It should do so now. Telephone markets have changed very rapidly in the 1980s, and will change more rapidly still in the 1990s. Rulemaking is a slow business in the best of circumstances, and rulemakers in

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<sup>95</sup>Responsive Comments of the FCC on the Report and Recommendations of the U.S. Concerning the Line of Business Restrictions at 63 (Apr. 27, 1987).


this business must move early if they are to keep abreast of technology and the market.

The Commission should accordingly take steps now to ensure an orderly transition to full competition in the marketplace for interLATA services. The Bell Companies ask the Commission to reaffirm its conclusion that BOC provision of interLATA services is in the public interest, and to establish the terms and conditions under which full competition may unfold.

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